



**7<sup>th</sup> EUROPEAN ROUNDTABLE ON CLEANER PRODUCTION  
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**PROMOTING FINANCING OF CLEANER PRODUCTION INVESTMENTS –  
UNEP EXPERIENCE**

**ABSTRACT**

The paper provides a summary of a recently completed study by UNEP/DTIE on past investment practices in cleaner production. It also provides a brief on the conclusions and recommendations of the debate that culminated at the parallel session on financing issues at the 6<sup>th</sup> International High-Level Seminar on CP, held in Montreal in October 2000. The paper then extracts the most relevant and topical issues from these papers and puts them into context of the European Roundtable on CP and beyond.

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**1. Introduction**

Is an end-of-pipe solution an investment with economic return or an expense? Is the actual cost of waste related to an investment project reflected in the calculations or is it hidden in company overhead accounts? Are preventative criteria embedded in the environmental impact assessments required by lenders?

These are the types of questions that dominate the current discussion on issues related to financing cleaner production investments. To address these issues, UNEP started implementing project 'Strategies and mechanisms for promoting cleaner production investments in developing countries' in 1999 with financial support from Norway. The project aims at understanding reasons for constraints faced by enterprises choosing the CP strategy in securing external funds for investments and at developing instruments to alleviate those constraints. In addition to global activities, the project has extensive field activities in five countries in three regions.

This paper summarises some of the outcomes and lessons learned in implementing the project and in recent fora where this issue has been debated. It then outlines the main

issues related to financing for discussion at the ERCF and the key challenges for the immediate future.

## **2. Study on past investment practices**

A study on past investment practices was conducted in eight countries and among global financial institutions in 1999 and early 2000. The countries studied include the five pilot countries of the project: Guatemala, Nicaragua, Tanzania, Vietnam and Zimbabwe, and three others to allow for comparison: India, Lithuania and Mexico. A full report of the study was published in November 2000.

The *overarching conclusions of the study*, applicable to all countries, can be grouped under three main headings:

### *i. Language*

The level of response to the global survey was exceedingly low. Language for 'cleaner production' has not been embedded in the financial services industry in the same way as 'environmental management'. There is a lack of clear understanding of the CP concept and misunderstandings or misinterpretations regarding its purpose. This language barrier was also evidenced at the national level where there were clear differences in the 'boundary conditions' for CP investment descriptions. The flexibility of interpretation is to be encouraged, it promotes innovation, extends the boundaries of environmental management to sustainable development policies and practices, and engages a wider level of societal input than would otherwise be the case.

### *ii. Time scales*

The process of initiating a CP assessment of a production process or potential design change is generally quite swift. Ensuing recommendations requiring little capital investment are normally implemented quickly. However, in cases where the CP concept is integrated into the capital budgeting process, a much longer time frame is required. Empirical evidence confirms that the period between loan agreement and disbursement is a significant barrier.

### *iii. Size of investments*

The danger is that where the CP component of an investment is justified separately, it is seen as an additional rather than an integral part of the project. This has the consequence of isolating CP investment as a hybrid rather than a mainstream embedded issue. Clearly best results can be achieved, if the process changes incorporating CP investment is valued as a whole.

In addition, each of the individual *country sections* of the study report incorporates national conclusions, based on the CP project analysis and financial institutions review, together with relevant recommendations. In the following, some *interesting findings*

*relevant to one or several of the studied countries* is provided. Each of these issues could be made subject to a special session and further elaboration.

- In many developing countries bank loans are considered unattractive due to high interest rates and unattractive terms of loans. Most companies require low interest, long term loans for environmental projects. Furthermore, the procedure for borrowing money from commercial banks is often considered complicated and costly.
- In many banks the due diligence process considers mainly the financial aspect of loan applications without paying much heed to technical ones. However, in some countries environmental considerations and sustainable development are gradually beginning to be translated into financial markets. Although many financial institutions are familiar with environmental opportunities, environmental investments remain small. Forthcoming environmental funding programmes (such as the World Bank Carbon Fund) are seen as new opportunities.
- Current efforts in promoting and implementing CP mostly concentrate on developing and adapting technology to existing production plants. In the future, the focus will eventually involve ‘technological leaps’ or technique transfer. This will require a shift to fundamental changes in the production plant, composition of raw materials and intermediary products, product design, etc. The size and magnitude of the CP projects will begin to reflect the change that is taking place during this transition. Consequently, this will have significant implications to the financing requirements for industry.
- So far, government policies have focused mainly on the tools for enforcing and extending compliance. The challenge for the governments will be to create a framework that provides incentives for companies to move beyond compliance and to take up CP as an efficiency measure.
- Policies introduced in some countries have highlighted the importance of favouring the adoption of environmental technologies with tax breaks e.g. on the importation and use of contamination-control equipment. Equally, the establishment of a similar policy focusing predominately on CP technologies and techniques could highlight the advantages over end-of-pipe.
- The ability to purchase appropriate machinery and equipment to support the CP concept has proven difficult for businesses.
- In some countries, the greatest potential for CP is the inflow of foreign direct investment (FDI) which can stimulate further new investment through downstream or upstream production. In this sense FDI can contribute to capital formation and job creation.

This study has highlighted some *key recommendations* for the adoption of cleaner production investments world-wide. These include:

- The need for governments to signal change with regard to national strategies that embrace cleaner production
- The need for industry to take up the challenge of creating an on-going demand for cleaner production measures that will spur continued progress
- The need for educationalists to integrate such thinking into the formal education programme
- The need for the financial services sector to identify cleaner production as an investment opportunity through financial innovation.

In doing so, the authors of the study believe that the long-term goal will be to pursue the introduction of cleaner production by every industry as a way of triggering a world-wide transformation of industrial practice and philosophy.

### **3. Sixth International High-Level Seminar on Cleaner Production (CP6)**

During the CP6, held in Montreal, Canada, 16-17 October 2000, a parallel session on financing issues was organised. The discussion was based on a background paper prepared by UNEP/DTIE and panelists from government agencies in Tanzania and Thailand, the World Bank, CAF, Rabobank and KPMG presented their own views. After a general debate, the following conclusions and recommendations can be made:

#### Conclusions

- There has been considerable progress in the implementation of CP investments from companies' own resources. A communication gap, however, remains between demand for external funding and their sources.
- Language can be a major barrier in introducing the CP concept to new audiences. It is also crucial in meeting the criteria of specific funds or facilities for CP investments. It is, however, less of a problem at the level of commercial investment projects.
- CP investments require a basic capacity level in a country, as without that there is very little demand in industry for CP implementation and little assistance available to those firms that do become interested in CP. This is a prerequisite for choice of countries of active CP investment promotion initiatives.
- There are examples of successful special funds for environmental and/or CP investments, but it is recognised that the process of integration into the financial market requires a certain period of time.

#### Recommendations

- CP should be embedded in government policies to encourage commercially competitive CP investments and to discourage perverse subsidies.
- Accounting practices in enterprises should be improved to reflect more accurately the actual cost of waste management and external environmental costs.

- Concerted efforts are needed to strengthen the capacity of financial institutions, business schools, academia and the media to understand the benefits of preventive approaches.
- Enterprises, particularly SMEs, need to be trained to prepare creditworthy investment proposals.
- Revolving funds and other targeted investment facilities should be encouraged to jump-start the implementation of bankable CP investments particularly in developing countries.

#### 4. ERCP and beyond

As can be concluded from the above summary, the analysis of constraints in cleaner production financing has evolved considerably in recent months and focus on specific issues is emerging. Their relevance to the ERCP can be summarised as follows:

- The number of *stakeholders* in activities related to the promotion of CP investment financing goes well beyond those that are customarily linked to the dialogue on CP proper. This should reflect in more active participation at CP roundtables of financial institutions and academia with curricula on financial analysis, business planning, accounting and engineering. An example of this expansion of CP to new groups of stakeholders is the interest shown by private banks to the presentation made on CP financing at the UNEP Finance Initiatives Annual International Roundtable in Frankfurt 16-17 November 2000.
- Need to develop a *definition of a CP investment*. This would address the issue of language which has been identified by the study on past investment practices and the CP6 parallel session as a key constraint. Some proposals were presented in the UNEP/DTIE background paper to CP6. It is hoped that the ERCP would also contribute to this debate.
- Knowing the *costs of processes* is vital for establishing what we might save by doing something in a different way. What you can measure, you can manage. CP needs to be mainstreamed into the due diligence process for preparing and assessing investment proposals. Within the framework of work carried out by the United Nations Division for Sustainable Development (UN-DESA), a process is currently underway to improve the role of government in promoting *environmental management accounting* (EMA). Partly the same group of international experts has designed training programmes for the UNEP/DTIE project on CP financing for field implementation. These experts will present their most recent findings at ERCP with a view to promoting wider use and greater harmony in the accounting practices with a CP bias.
- The need for *training and capacity building* has clearly emerged as an important element in the above summaries. Based on field analysis of training needs and a review of available global expertise, UNEP/DTIE has embarked on a process of designing four distinct training programmes for large-scale implementation in the five

pilot countries of the CP financing project. The objectives and contents of the programmes will be presented to the ERCP at a separate session with a view to improving on them based on feedback from practitioners and ultimately adaptation and use also in the European context.

- The role of *financial institutions* is naturally crucial. Some have established revolving funds and special credit lines for CP investments, with varying results. Some others are beginning to include CP into their training of financial intermediaries. Some others do not pay attention to CP as such, but have a more general environmental focus. *Governments* has a key role in creating a policy and regulatory environment conducive to the adoption of preventive strategies in business. A special panel discussion is arranged at the ERCP to review different approaches adopted by selected financial institutions with a view to drawing conclusions at the level of banks and to recommending policies and strategies for governments to consider.

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